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IN THE

Supreme Court of the United States

October Term, 1941

NO. 760

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ESTATE OF JOHN SAGE, DECEASED, ALFRED D. SAGE, ROBERT J. RENDALL AND THE FIFTH AVENUE BANK OF NEW YORK, EXECUTORS, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF

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IN THE

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OCTOBER TERM, 1941

No.

ESTATE OF JOHN SAGE, DECEASED, ALFRED D. SAGE, ROBERT J. RENDALL and THE FIFTH AVENUE BANK OF NEW YORK, Executors, Petitioners

v.

COMMISSIONER OF INTERNAL REVENUE

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

The petition of Alfred D. Sage, Robert J. Rendall and The Fifth Avenue Bank of New York, executors of the last will and testament of John Sage, deceased, respectfully shows:

The Question Presented

The only question involved is whether, in computing the federal estate tax, the amount deducted by the executors of

a decedent's last will and testament for charitable and public bequests must be reduced by a sum equivalent to the amount agreed to be paid by the residuary charitable beneficiary to or for the decedent's widow, under an agreement in settlement of a contest over the probate of the decedent's last will and testament.

Summary Statement of Matter Involved

This petition for a writ of certiorari seeks to review a decision of the Circuit Court of Appeals for the Third Circuit (R. 79, 87) affirming a decision of the Board of Tax Appeals (R. 40), which sustained the Commissioner's determination of a deficiency in federal estate tax in the sum of $9,687.66. The issue arises under Sec. 303 (a) (3) of the Revenue Act of 1926 (44 Stat. 72, 26 U.S.C.A. § 412), as amended. The stipulated facts (R. 48) are as follows:

Petitioners are the executors of the estate of John Sage, who died on October 11, 1936, testate, a resident of Bergen County, New Jersey. He left him surviving a widow, Dorothy T. Sage. On December 21, 1936, she was adjudged an incompetent, and thereafter guardians were appointed for her by the Bergen County Orphans' Court.

The decedent left an estate of approximately $450,000.00. Under his last will and testament (R. 51), his widow was bequeathed his household effects and legacies totaling $42,000.00. The residuary estate was bequeathed to the Lord Provost of Glasgow, Scotland, in manner following:

> "ELEVENTH: I direct my said executors to convert into cash all the rest, residue and remainder of my property of whatsoever kind, nature or description, and I give and bequeath the proceeds of such conversion to the LORD PROVOST of Glas-

gow, Scotland. I request said LORD PROVOST to distribute same among such institutions in Scotland, as are devoted to the care and maintenance of blind, maimed and disabled soldiers and sailors of the British Army and Navy, according to his best judgment and discretion."

The will was first offered for probate in New York, where its admission was contested by the widow. The New York proceedings were subsequently dismissed, and the will was offered for probate before the Surrogate of Bergen County, New Jersey, on April 9, 1937. On May 8, 1937, the widow's guardians entered into an agreement with the Lord Provost, through his attorney-in-fact (R. 55). In substance, this agreement provided that the widow, through her guardians, would withdraw all objections to probate and that the Lord Provost, as residuary legatee would pay to the widow a sum equivalent to 25% of the amount received by the residuary legatee under the provisions of the will (R. 35, 80). Petitioners, as executors, were not parties to this agreement. Thereafter, upon the petition of the guardians (R. 65), this agreement was approved by the Bergen County Orphans' Court (R. 73). The agreement was not, however, incorporated in, nor did it ever become a part of, the probate or other proceedings relating to the administration and distribution of the decedent's estate. Its approval was made necessary only because it concerned the acts of guardians in behalf of an incompetent.

Thereupon, all objections in behalf of the widow to the probate of the will were discontinued and it was admitted to probate on May 19, 1937. Petitioners thereupon qualified as executors and entered upon the administration of the estate.

On December 1, 1937, petitioners rendered their final account as executors to the Bergen County Orphans' Court. On January 11, 1938, the account was allowed (R. 74). The account showed a balance for distribution of $175,750.48, after the payment of debts, specific and general legacies and allowances, and the payment of all commissions, counsel fees and other administration expenses and disbursements. Thereafter, on February 9, 1938, a decree of distribution was entered, which awarded and distributed the entire balance on hand to the Lord Provost as residuary legatee. Neither this decree nor that allowing the account provided for any payment to the widow, or her guardians, other than to approve the earlier payment and delivery to her of the cash legacies of $42,000.00 and the decedent's household effects.

On March 30, 1938, the attorney-in-fact for the Lord Provost, pursuant to the terms of the compromise agreement, paid the sum of $33,687.62 to the widow's guardians and, at the time of the stipulation before the Board of Tax Appeals, had in his possession the further sum of $5,000.00 to be paid to the widow's guardians.

On September 20, 1937, petitioners filed a federal estate tax return in which deduction was claimed for the full amount of the residuary estate as a charitable and public bequest. On January 5, 1939, the Commissioner determined a deficiency in tax, having disallowed one-fourth of the deduction claimed for the residuary bequest on the ground that, under the terms of the compromise agreement, the amount paid the widow by the Lord Provost passed to her, as the widow, in settlement of her contest of the will, and that , in no event, could the payment to the widow be considered part of a charitable bequest entitled to freedom from estate tax. The State of New Jersey had previously assessed the decedent's estate for

transfer inheritance taxes on the basis that the entire residuary estate was a charitable and public bequest.

It has been conceded throughout that the residuary bequest was to a charitable use. It is only the amount which may be deducted in determining the net estate subject to tax which is in dispute. It has been further admitted throughout that neither petitioners, the charitable beneficiary nor the widow's guardians entered into the agreement in question to evade, or to affect in any way, the tax liability of the estate, the agreement having been consummated prior to the decisions in any of the cases discussed by the tribunals below.

The Circuit Court of Appeals, in affirming the decision of the Board of Tax Appeals, held as follows:

1. The widow took from the estate that which she received under the compromise agreement, not by testacy or intestacy, but by a novel category of succession which the court called "inheritance". The principles of the income tax case of *Lyeth* v. *Hoey*, 305 U. S. 188, were applied to the situation.

2. The decision in the similar case of *Robbins* v. *Commissioner*, 111 Fed. (2d) 828 (C. C. A. 1st), relied upon by petitioners, was not followed. The reasoning of the *Robbins* opinion that the *Lyeth Case* is not applicable to estate tax problems and that taxability must be determined by the situation existing at the date of death was ignored and inferentially disapproved.

3. Sec. 303 (a) (3) of the statute must be read to mean that the deduction, in the case of a bequest to a trustee for a charitable use, is measured by the amount which the charity actually receives and uses for charitable purposes and not by what the testator provided.

4. Sec. 303 (a) (3) of the statute must be read to mean that some part, or all, of a deductible charitable bequest

may be rendered taxable by the acts of persons, other than the executor, in settling a will contest subsequent to death and irrespective of the testator's expressed intentions.

The opinion of the Board of Tax Appeals is reported in 42 B. T. A. 1304 (R. 33) and that of the Circuit Court of Appeals in 122 Fed. (2d) 480 (R. 79).

Jurisdiction

The judgment of the Circuit Court of Appeals was entered June 27, 1941 (R. 87). On September 18, 1941, this Court extended the time within which petitioners could file a petition for a writ of certiorari to November 26, 1941 (R. 89).

Jurisdiction to issue the writ is found in the provisions of Sec. 240 (a) of the Judicial Code, as amended, (43 Stat. 938, 28 U. S. C. A. § 347).

Reasons Relied upon for Allowance of the Writ of Certiorari

A writ of certiorari should be allowed because:

1. This case presents a novel, substantial and important federal tax question relating to the construction of Sec. 303 (a) (3) of the Revenue Act of 1926, as amended, which has never been passed upon by this Court. An early authoritative decision by this Court of this question, to wit: whether, in computing the federal estate tax, the amount of the deduction for a charitable and public bequest must be reduced by a sum equivalent to the amount paid, or agreed to be paid, by the charitable beneficiary to a decedent's widow, or other "heirs", under an agreement in settlement of a probate contest, is of pressing

importance, not only to the parties to this cause, but also to all persons whose estates may be subject to federal estate taxes and those who may be required to administer such estates as executors. The precise question has been before the Commissioner on numerous occasions and has just again been decided adversely to the executor, on the basis of this case, by the Circuit Court of Appeals for the Second Circuit in *Thompson* v. *Commissioner* (No. 39, October Term, 1941, decided November 17, 1941 and not yet reported), a case involving a deficiency assessment of more than $120,000.00 and in which, petitioners are informed, application will be made to this Court for a writ of certiorari.

2. Aside from the novelty and importance of the issue presented, the decision below is erroneous and not in accord with the principles of the following decisions of this Court, to wit: *United States* v. *Provident Trust Co.*, 291 U. S. 272; *Edwards* v. *Slocum*, 264 U. S. 61; *Y. M. C. A.* v. *Davis*, 264 U. S. 47; *New York Trust Company* v. *Eisner*, 256 U. S. 345, 348, 349, and *Knowlton* v. *Moore*, 178 U. S. 41, 49, in that it disregards the fundamental rules laid down therein that (a) the federal estate tax is one on transmission and not on succession, (b) is governed by the situation existing at the testator's death and (c) is controlled by what he did in his will, in the absence of a statutory exception thereto. No exception concerning amounts paid, or agreed to be paid, by charitable beneficiaries in settlements of probate contests effected subsequent to the testator's death is found in Sec. 303 (a), nor was relied upon by the court below.

3. The decision below is in conflict with the reasoning of the Circuit Court of Appeals for the First Circuit in *Robbins* v. *Commissioner*, 111 Fed. (2d) 828, where it was held, in a case involving a similar estate tax prob-

lem, that the rationale of *Lyeth* v. *Hoey, supra,* is not applicable to estate tax cases and that deductions for charitable bequests must be determined by the situation existing at the date of death. This irreconcilable state of the reasoning in the authorities on the question of the construction of Sec. 303 (a) (3) aforesaid, in the absence of a clarifying adjudication by this Court, leaves the law in uncertainty.

4. The court below erred in basing its decision upon the income tax case of *Lyeth* v. *Hoey, supra,* in that it held that the widow took the amount of her compromise, not by testacy or intestacy, but by "inheritance", a term not found in the applicable provisions of the estate tax law as it is in Sec. 22 (b) (3) of the Revenue Act of 1932 dealing with certain exemptions from income tax. This is a clear misapplication of the principle of the *Lyeth Case.* The broad language used in the *Lyeth* opinion has resulted, as here, in confusion and unsound application and should be limited by this Court to the facts and statute there involved.

5. The court below, in its construction of Sec. 303 (a) (3) on a phase never passed upon by this Court, erred in holding that that section must be read to mean (a) that the amount deductible is the amount actually received and used by the charitable beneficiary for charitable uses, irrespective of the provisions of the testator's will and of agreements made in settlement of will contests to which the executors are not parties and of which they may not even have knowledge; (b) that where such charitable beneficiary is a trustee, as distinct from a charitable corporation, the section imposes a stricter test of deductibility; and (c) that Art. 47 of Treasury Regulations 80 concerning conditional charitable bequests is applicable despite its clear language to the contrary.

6. The court below, in its construction of Sec. 303 (a) (3), invaded the Congressional field of legislation, since the statute is entirely silent on the question of any exception to deductibility where the charitable beneficiary pays, or agrees to pay, a sum in settlement of a will contest. Congress not having covered the situation and there being no reasonable basis of interpretation to be derived from the legislation to cover it, the statute must be construed liberally in favor of the taxpayer and the deduction allowed in the full amount of the charitable bequest as made by the testator.

WHEREFORE, your petitioners respectfully pray that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals for the Third Circuit, commanding that court to certify and to send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and all proceedings therein; and that the said judgment of the United States Circuit Court of Appeals for the Third Circuit may be reversed by this Honorable Court, and that your petitioners may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

T. Girard Wharton,
Counsel for Petitioners.

Dated November 24, 1941.